

## **CALIFORNIA LITIGATION:**

***Featured Article, Volume 12, Number 3, 1999***

### **Alternative Dispute Resolution: Pitfalls in Drafting the Agreement — Is It Fish or Fowl?**

By The Honorable William E. Rylaarsdam

Perhaps following some arm twisting by the settlement conference judge, you have agreed to submit your case or some of the issues to alternative dispute resolution. You and your opponent agree on a "referee" to conduct the proceedings and agree the arbitration will take place at your opponent's office. You incorporate the terms of your agreement in a writing which then provides the proceedings will be conducted before a designated "temporary judge" under the American Arbitration Association's rules for Commercial Arbitration. What are the implications of what you have agreed to do with your client's case? As illustrated by a number of cases that have reached our appellate courts in the last few years — some of them resulting in published opinions — you have probably agreed to something other than what you intended. You and your opponent have created a chimera, a monster that is neither fish nor fowl.

Parties may stipulate to contractual arbitration, judicial arbitration, a reference under Code of Civil Procedure section 638, or to the appointment of a temporary judge under California Constitution, Article VI, section 21. Each of these procedures has distinct characteristics and the scope of judicial review of the decision rendered is different for each of them.

Judicial review of an award following contractual arbitration has been extremely limited since the California Supreme Court decided *Moncharsh v. Heily & Blase* 3 Cal.4th 1 (1992). Arbitrators do not have to follow the law or the rules of evidence. The only attacks available to a party dissatisfied with the arbitrator's decision are those authorized in Code of Civil Procedure sections 1286.2 and 1286.6, involving such issues as corruption of the arbitrator. An error of law, even if it appears on the face of the award, does not entitle a party to a reversal. This is true even for errors "causing substantial injustice," a ground for reversal permitted by cases which preceded the *Moncharsh* decision.

Judicial arbitration pursuant to Code of Civil Procedure sections 1141.10 et seq., on the other hand, is never conclusive unless the parties expressly stipulate to the contrary. Parties dissatisfied with the result of such arbitrations are entitled to trials *de novo*, subject to certain penalties if they fail to obtain a better result at trial. The judgment after trial is, of course, fully appealable.

Code of Civil Procedure section 638 permits the court, upon a stipulation by the parties, to order a reference. The Parties are entitled to a statement of decision. In a general reference, the decision of the referee is the decision of the court and "may be excepted to and reviewed in like manner as if made by the court." (Code Civ. Proc., § 645.) The trial court may grant a motion for a new trial and vacate the award of the referee to the same extent as if the judge had heard the matter. In a special reference, the referee merely makes a recommendation to the trial judge, which the latter may accept, reject, or modify. A judgment following either kind of reference is fully appealable. Finally, California Constitution, Article VI, section 21, provides that "[o]n stipulation of the parties litigant the court may order a cause to be tried by a temporary judge who is a member of the State Bar, sworn and empowered to act until final determination of the cause." California Rules of Court, rules 244 and 532, spell out the procedures to be followed before such a stipulation can be effective. They include requirements that temporary judges take an oath of office and that the presiding judge of the court; or the supervising judge of a branch, approves their appointment. Such judges act in all respects under the same rules as constitutional trial judges and their judgments are subject to the same level of appellate review as any others.

Thus, each of these procedures is different and an agreement for alternative dispute resolution has different legal consequences depending on which is selected. However, there is no precedent which permits courts to deal with hybrids. When the agreement between the parties purports to combine the characteristics of two or more alternative dispute resolution procedures, the court must select one of these and results unintended by either side may obtain. Our district of the Court of Appeal has recently encountered several cases where the parties' agreement failed to clearly indicate which form of alternative dispute resolution was intended. We were forced to choose between the defined forms. This probably resulted in neither party obtaining what it bargained for.

In *Old Republic v. St. Paul Fire & Marine Ins. Co.* 45 Cal.App.4th 631 (1996), two insurance companies disputing coverage for an accident involving a truck and trailer, one carrier insuring the truck, the other the trailer, entered into a "Stipulation for Binding Arbitration Before Special Master." The stipulation specified that the arbitration was to be governed by California Rules of Court for judicial arbitrations. (Code Civ. Proc., §§ 1141.10 - 1141.31; Cal. Rules of Court, rules 1600 - 1618.) The decision of the "special master," including his findings of fact and conclusions of law, were agreed to constitute the judgment, subject to trial court review under the statutes dealing with contractual arbitration. (Code of Civ. Proc. §§ 1280 - 1288.8). Finally, the stipulation provided that the judgment would be subject to appellate review to the same extent as if it had been rendered after a bench trial. (Code of Civ. Proc., § 904.1, subd. 1).

As is usually the case, one of the parties to the stipulation was dissatisfied with the award issued by the "special master" and appealed from the judgment entered in accordance with the stipulation. Although the stipulation clearly contemplated plenary appellate review and neither party disputed the power of Court of Appeal to hear the case, the court concluded it lacked jurisdiction to consider the appeal.

Based on the language of the stipulation, the *Old Republic* court concluded that, although some inconsistent terms had been used, the substance of the agreement, and particularly the provision limiting the power of the trial court to review the award under the statutes for contractual arbitration, constituted a stipulation for contractual arbitration. By depriving the trial court of the full scope of review permitted for the award of a special master, whose decision would have been appealable, the parties, in effect, had sought to shift a task constitutionally assigned to the trial court, to the Court of Appeal. This they could not do; where the appellate court lacked jurisdiction, the parties could not confer such jurisdiction by their stipulation.

In *Sy First Family Ltd. Partnership v. Cheung* 70 Cal.App.4th 1334 (1999) the parties labeled their stipulation a "Reference to American Arbitration Association" and referred to the section of the Code of Civil Procedure relating to references by consent of the parties. (Code Civ. Proc., § 638.) The stipulation further provided that three "arbitrators" would conduct the "trial" in accordance with "the Association's Commercial Rules of Arbitration."

During a preliminary hearing, the "arbitrators" inquired what the nature of the proceedings was intended to be, a reference or an arbitration. The parties then submitted an equally confusing supplemental stipulation. Finally, the "arbitrators" announced that they would proceed with an arbitration; there was no objection and, after a hearing, the "arbitrators" issued an "award." The trial court concluded the parties had engaged in a reference, denied the successful party's motion to confirm the award, ordered the "referees" to issue a statement of decision, and subsequently entered judgment in accordance with this statement.

One of the parties appealed from this judgment. The appellate court concluded that the stipulation in fact constituted an agreement to arbitrate, reversed the trial court's denial of a petition to confirm the award and limited the scope of appeal to that single issue. One of the factors which motivated the appellate court was that the stipulation provided that the hearing would be conducted under the "Association's Commercial Arbitration Rules." The court noted: "Critical differences exist between the evidentiary and procedural rules applicable to a judicial proceeding and a hearing under the American Arbitration Association's Commercial Arbitration Rules. ...It is inappropriate for a court to review an arbitration decision issued after a hearing conducted under rules of evidence and procedure not applicable in courts of law."

It is not possible to design an arbitration agreement so as to preserve full appellate review. On the other hand, an agreement for a reference under Code of Civil Procedure section 638 or a judgment rendered by a

temporary judge may, and, unless the parties have stipulated to the contrary, does preserve such rights.

In *National Union Fire Ins. Co. v. Nationwide Ins. Co.* 69 Cal.App.4th 709 (1999), the parties had attempted to stipulate to a "binding arbitration...on the record and with all parties retaining their right to appeal." Later, realizing that there was no such animal, they prevailed upon the trial court to modify their stipulation "to constitute a reference by consent of the parties." The resulting judgment was held to be subject to appellate review.

*Elliott & Ten Eyck Partnership v. City of Long Beach* 57 Cal.App.4th 495 (1997) presents a situation where the parties discovered to their surprise that their agreement to arbitrate actually resulted in a trial before a judge with all the consequences which resulted from such a trial. There the parties had stipulated that a sitting judge decide the case "as an arbitrator, rendering a final decision not subject to appeal." The judge issued a "decision of arbitrator" and signed it as "arbitrator. " The parties followed the statutory procedure for confirmation of an arbitrator's award and the losing party appealed in spite of the contrary stipulation. The Court of Appeal decided that sitting judges cannot act in any capacity which relieves them from their constitutional obligation to follow the law and from acting as a judges. The court concluded that, in spite of the parties' stipulation and the judge's belief he was acting as an arbitrator rather than as a judge, they had actually been engaged in a bench trial.

Before entering into any agreement for alternative dispute resolution, counsel must understand the differences between the various procedures and the differing scopes of judicial and appellate review available after the determination of the decision-maker. Lawyers must advise their clients of these distinctions and the consequences that flow from them. Finally, counsel must draft their stipulations with such precision that no questions may arise as to the type of alternative dispute resolution selected.

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